No. 93-144

In The

Supreme Court of the United States

October Term, 1993

DEPARTMENT OF REVENUE OF THE STATE OF MONTANA,

Petitioner,

vs.

KURTH RANCH; KURTH HALLEY CATTLE COMPANY; RICHARD M. and JUDITH KURTH, husband and wife; DOUGLAS M. and RHONDA I. KURTH, husband and wife; CLAYTON H. and CINDY K. HALLEY, husband and wife; ROBERT G. DRUMMOND, TRUSTEE,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

REPLY BRIEF OF PETITIONER

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December 1993

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A. Introduction

The pivotal question in this case is whether Montana's Tax is a tax. The double jeopardy provision of the Fifth Amendment comes into play only if Montana seeks to punish the Taxpayers twice for the same offense. If, and only if, the Montana Tax is a sanction can the Court's decision in *United States v. Halper,* 490 U.S. 435 (1989) be applied to the tax assessment at issue.

The case involves a specific tax – a tax of $100 an ounce on the possession of marijuana. The tax assessment at issue is $181,100 for the possession and storage of 1,811 ounces of marijuana.[1]

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[1] The contention that imposition of the tax against all the Taxpayers was not proved at the trial is without merit. For example, the Agreed Facts in the Pre-Trial Order stated: "The Plaintiffs, in December, 1985 or January, 1986 began growing and selling marijuana." (Pet. App. 29) Also see Agreed Fact 15. (Pet. App. 29-30.) The Plaintiffs included Richard M. Kurth, Judith M. Kurth, Douglas M. Kurth, Rhonda I. Kurth, Clayton H. Halley, Cindy K. Halley, Kurth-Halley Cattle Company, and Kurth Ranch.

The evidence offered at the trial to support imposition of the tax on all the Taxpayers came from their testimony particularly that of Richard Kurth. (Tr. p. 74). His testimony was supported by depositions of other family members which were introduced into evidence. For example, Judith Kurth testified:

> Q. (B. McGinnis) Were you aware, Mrs. Kurth, that there was a marijuana growing operation conducted on that property?
>
> A. (J. Kurth) Yes.
>
> Q. (B. McGinnis) And were you involved with the growing operation?
>
> A. (J. Kurth) Yes, I was.

The Taxpayers' assertion that the record does not support this assessment and the Department's description of their marijuana operation and sales is without merit.[2]

(Judith Kurth Dep. p. 60) The evidence included a video tape of the marijuana operation (Exhibit DD).

That evidence supports imposition of the tax against all members of the Kurth family, the Kurth-Halley Cattle Company and the Kurth Ranch. This evidence supported the bankruptcy court's finding that the Department legally imposed a tax of $181,100 against all the Taxpayers. (Pet. App. 58). The Taxpayers did not cross-appeal those findings.

The remaining respondent, Robert Drummond, the bankruptcy trustee is not a party since the bankruptcy trustee accedes to the property rights of the Debtors and not to the individual constitutional rights of the Debtors. 11 U.S.C. § 110(a) and § 541

[2] For example, at the trial, this exchange took place between Richard Kurth and one of the Taxpayers' attorneys, Mr. Gallik:

> Q. (Gallik): At what quantities would you typically sell the bud?
>
> A. (Kurth): I'm going to say anywhere from three to I think at one point I sold as much as eight pounds to him. . . .
>
> Q. (Gallik): How much money did you receive for a pound of marijuana?
>
> A. (Kurth): When we first started, we got $1,000 per pound. And as the thing progressed, the second man, Dave Eggebrecht, informed us that was not a fair price to us, and the price moved up from $1,000 gradually up to where the last six months we got $1,800 a pound for bud.

(Tr. at 80.)

B. Montana's Tax Does Not Require Arrest Or Conviction.

The Taxpayers cite Mont. Code Ann. § 15-25-112 (1987) for the proposition that "liability for Montana's drug tax is tied directly to the commission of a crime and is conditioned upon the culpability of the 'taxpayer'." (Taxpayers' Brief at 34.) Montana Code Annotated § 15-25-112 (1987) states:

> The tax imposed pursuant to 15-25-111 does not apply to any person authorized by state or federal law to possess or store dangerous drugs. The burden of proof of an exemption from 15-25-111 is on the person claiming it.

This statute merely states that the tax is on illegal activity. The Department of Revenue has never denied that the tax is on an illegal activity. However, not every unauthorized possession of marijuana results in arrest let alone conviction.[3]

The Taxpayers cite Mont. Admin. R. 42.34.102(1) for the same proposition and for the proposition that "liability for the drug 'tax' does not arise – and cannot be paid – until the individual is arrested." (Taxpayers' Brief

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[3] A "person" is defined as "an individual, firm, association, corporation, partnership, or any other group or combination acting as a unit." Mont. Code Ann. § 15-25-102 (1987). Therefore, the tax can be applied to "persons" which are not arrested or charged with criminal possession of drugs, e.g., the Kurth-Halley Cattle Co., a partnership. If Kurth Ranch and Kurth-Halley Cattle Company were corporations, those corporations would be liable for the tax.

at 34.) This is not true. Montana Administrative Rule 42.34.102(1) states:

> Every person possessing or storing dangerous drugs, and not authorized to do so by law, shall file a return with the department. This return shall contain the type, quantity, and market value of such dangerous drugs in their possession or being stored by them. This return shall be filed within 72 hours of their arrest.

(Taxpayer App. p. 1). This rule does not require an arrest or a conviction in order to make a person liable for the tax. The rule acknowledges the tax is on an illegal activity and indicates that if an arrest occurs, a return must be filed. This is simply a common sense approach to collecting a tax on an illegal activity.

The Taxpayers' cite Mont. Admin. R. 42.34.109(1)(d) for the proposition that the drug taxes "may be included 'as an integral and contingent portion of any plea agreement' between the 'taxpayer' and the county attorney responsible for the criminal prosecution of the 'taxpayer.' " Taxpayers Brief at 34. That rule provides:

> (1) Upon their concurrence the department may seek the assistance of any court of competent jurisdiction, officer of the court or county attorney in collection of any assessment under the provision of this act by:
>
> . . .
>
> (d) requesting that upon notification of any assessment from the department the county attorney include payment of such assessment as an integral and contingent portion of any plea bargain agreement with the taxpayer.

Again, this rule merely provides a practical approach to the collection of the tax. The rule does not indicate that an arrest or conviction is required for a person to be liable for the tax.

Finally, the Taxpayers failed to call to the Court's attention one of the Administrative Rules for the Drug Tax, Mont. Admin. R. 42.34.105 which states: "(1) A criminal conviction for drug related charges or other charges is not a prerequisite for the tax." (Taxpayer App. 4)

C. The *LaFranca* Decision is Not Controlling – the Decision is Not Precedent in Light of Subsequent Decisions and did not involve Double Jeopardy.

The Taxpayers argue that this case is controlled by *United States v. LaFranca*, 282 U.S. 568 (1931). In *LaFranca* the Court stated:

> A tax is an enforced contribution to provide for the support of government; a penalty, as the word is here used, is an exaction imposed by statute as punishment for an unlawful act. The two words are not interchangeable, one for the other. No mere exercise of the art of lexicography can alter the essential nature of an act or a thing; and if an exaction be clearly a penalty it cannot be converted into a tax by the simple expedient of calling it such.

Id. at 572. No one has contested this principle.

However, the decision in *LaFranca* that pursuant to *Lipke v. Lederer*, 259 U.S. 557 (1922) "the exaction here in question is not a true tax, but a penalty involving the idea of punishment for infraction of the law" is of doubtful

value as precedent. *LaFranca*, 282 U.S. at 572. In *Bob Jones University v. Simon*, 416 U.S. 725, 743 n.12 (1974), the Court abandoned the *Lipke* analysis on which *LaFranca* was based:

> In support of its argument that this case does not involve a "tax" within the meaning of § 7421(a), petitioner cites such cases as *Hill v. Wallace*, 259 U.S. 44, 42 S.Ct. 453, 66 L.Ed. 822 (1922) (tax on unregulated sales of commodities futures) and *Lipke v. Lederer*, 259 U.S. 557, 42 S.Ct. 549, 66 L.Ed. 1061 (1922) (tax on unlawful sales of liquor). It is true that the Court in those cases drew what it saw at the time as distinctions between regulatory and revenue raising taxes. *But the Court has subsequently abandoned such distinctions.* E.g., *Sonzinsky v. United States*, 300 U.S. 554, 81 L.Ed. 772 (1937). (Emphasis supplied.)

The *LaFranca* decision is further placed in question by the Court's decision in *Helvering v. Mitchell*, 303 U.S. 391 (1938). In that case, based on *LaFranca*, the circuit court held that the imposition of an additional 50% assessment of $364,354.92 against a taxpayer because he committed fraud was barred under double jeopardy because of a prior acquittal on criminal charges involving the same fraud. The tax and 50% fraud assessment totalled $1,093,064.78. The Court reversed the circuit court and affirmed the additional assessment. In *Mitchell* the Court rejected double jeopardy arguments similar to those raised by the Taxpayers in this case. *Id.* at 393. *Mitchell* also demonstrates that if the sanction is statutorily

proportional to the sanctioned activity there is no double jeopardy difficulty.

As the Court noted in *Halper*, *LaFranca* did not even address any double jeopardy question.[4] Rather the Court based the decision in construction of the statute at issue.[5] Thus, contrary to Taxpayers' assertions on page 7 of their brief, in *LaFranca* the Court did not reject "the government's argument that the second measure was a civil tax rather than punishment under double jeopardy."

D. The Taxpayer Ignored the Careful Statutory Analysis of the Tax by the Montana Supreme Court – in Contrast the Circuit Court failed to analyze the Tax.

No one is arguing that labeling a statute a "tax" immunizes a statute from the Court's review just as alleging a tax is a "penalty" does not make it a penalty. The Montana Supreme Court in *Sorenson v. State Department of Revenue*, 836 P.2d 29 (Mont. 1992) certainly did not view the Montana Tax as "immune from judicial review." Instead, it conducted full analysis of the statute prior to concluding it was a tax.[6]

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[4] "See also *United States v. LaFranca*, 282 U.S. 568, 573 (1931) (asking, but not answering whether a penalty assessed in a civil proceeding may nonetheless constitute punishment for the purposes of double jeopardy analysis)." *Halper*, 490 U.S. at 443.

[5] Also see *Wainer v. United States*, 299 U.S. 92 (1936) which was decided after *LaFranca*. In that case the Court upheld a criminal conviction for failure to pay the special tax at issue in *LaFranca*.

[6] The Taxpayers faulted the Montana Supreme Court's *Sorenson* decision for using "the wrong legal analysis when it

In contrast, the circuit court held that *Halper* requires a determination of the relationship between the tax imposed by the state and damages suffered by the government without analyzing whether or not the tax assessment was a civil penalty, or even whether it was remedial. Instead, the circuit court placed the burden on the state to demonstrate that the tax assessment was proportional to the "actual damages and costs." (Pet. App. at 11). The court short-circuited the *Halper* analysis by assuming that a tax assessment is a civil sanction, and further, that requiring a person to pay over $181,000 was so grossly disproportionate that it required a finding that the tax was punitive.

The circuit court never considered the statute itself, the expressed legislative purpose of the tax statute, the legislative history, or the history of similar federal taxes but only looked to the size of the assessment. The circuit court ignored the fact that the assessment was large because the Taxpayers had a large amount of marijuana – the tax was proportional to the amount of the taxed commodity. The circuit court apparently adopted the position advocated by the Taxpayer that an ostensibly large tax assessment undermines all other factors including any remedial purpose. Therefore, its opinion conflicts with numerous decisions by this Court.

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relied upon *Kennedy v. Mendoza-Martinez*, 373 U.S. 144 (1963) and *United States v. Ward*, 448 U.S. 242 (1980). Taxpayers' Brief at 42. Yet, the Taxpayers cite with approval the analysis of the bankruptcy court which was based on the same *Kennedy v. Mendoza-Martinez* test. Taxpayers's Brief at 38-39. (Pet. App. at 54 and 58-59)

E. The Purpose of the Montana Tax is Neither Deterrence Nor Retribution.

The Montana Tax itself, the preamble, and the legislative history show no indication that the tax had a retributive or deterrent purpose nor can such purposes be implied. It is inconceivable that anyone would believe that drug dealers who are not deterred by the severe federal and state criminal penalties would be deterred by a tax on marijuana. See *Harmelin v. Michigan*, 115 L. Ed. 2d 836 (1991) (Life imprisonment for possession of cocaine.) The Taxpayers planned to net over a million dollars a year from growing marijuana.[7] A tax of $181,000 does not seem unreasonable in light of these profits.

The Montana Tax, the preamble, and the legislative history do not indicate any retributive intent. The intent of the tax is to raise money for governmental services closely linked to the taxed activity.

Contrary to the Taxpayers' argument the fact that the Montana Tax funds specific governmental programs related to drugs does not change its fundamental character as a tax. There are numerous excise taxes with revenues dedicated to specific programs associated with the taxed commodity, e.g., the federal excise tax on coal

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[7] Q. (Van Tricht) How much did you owe the bank? . . .

A. (R. Kurth) Between the two banks, Norwest Bank and the Land Bank, about $2 million.

Q. (Van Tricht) You planned to pay them off with the production of marijuana within two years?

A. (R. Kurth) Yes.

Tr. p. 107.

funds the black lung disability program (26 U.S.C. § 4121), the excise tax on aviation fuel funds airport construction (26 U.S.C. § 4091), and the federal excise tax on chemicals funds environmental clean up ("the superfund") (26 U.S.C. § 4611). Those federal taxes are just as much a tax as the federal income tax which raises revenue for general governmental purposes.

As the Court noted in *Halper*, whether a civil penalty is a punishment cannot "be determined from the defendant's perspective." "On the contrary, our cases have acknowledged that for the defendant even remedial sanctions carry the sting of punishment." *Id.* 490 U.S. 447 n. 7. The Montana Tax is $100 an ounce; a level approved by federal courts in the cases previously cited. It is not $1,000 an ounce or $10,000 an ounce. The Court does not address "hypothetical or contingent questions." *Alabama State Federation of Labor v. McAdory*, 325 U.S. 450, 461 (1945). The assertion that a tax can be raised so high as to be unconstitutional does not make an existing much lower tax unconstitutional.

F. The Court has Repeatedly Approved Excise Taxes on Illegal Products.

The Taxpayers fuse the two issues of whether the Montana Tax is truly a tax or a sanction and whether, if a sanction, the tax is punitive rather than remedial. The first issue is whether the Montana Tax is a sanction. The second issue is if the tax is a sanction does it constitute a punishment for the purposes of the Double Jeopardy Clause. The Court's decision in *Halper* makes it clear that

all sanctions are not punishment under the Double Jeopardy Clause. *Halper*, 490 U.S. at 446.

The Taxpayers wrongly imply that merely taxing a criminal activity automatically makes a tax a sanction. The Court has approved taxing illegal activity at least since the *License Tax Cases*, 5 Wall 462 (1866). That case involved a tax on lotteries which at that time was an illegal activity. This Court has approved taxes conditioned on illegal activities. For example, the Court approved the taxation of intoxicating spirits during prohibition. In *United States v. One Ford Coupe Auto.*, 272 U.S. 321, 328 (1926), the Court held:

> The claimant contends that the so-called tax on illicitly distilled spirits theretofore imposed ceased to be a tax and became in law a penalty, when the enactment of the National Prohibition Act changed the purpose of the tax from raising revenue to preventing manufacture, sale, and transportation; and that to enforce such penalty by forfeiture of the property rights of innocent third parties would be a denial of due process of law. It is true that the use of the word "tax" in imposing a financial burden does not prove conclusively that the burden imposed is a tax; and that when it appears from its very nature that the imposition prescribed is a penalty solely, it must be treated in law as such. But the imposition here in question is not of that character. *A tax on intoxicating liquor does not cease to be such because the sovereign has declared that none shall be manufactured, and because the main purpose in retaining the tax is to make law-breaking less profitable.* (Emphasis supplied.)

Also included among the approved taxes on illegal activity was a federal tax on wagering, an illegal activity at the time. See *United States v. Kahriger,* 345 U.S. 22 (1954). The tax was conditioned on commission of a crime.

Contrary to the Taxpayers' contention, *Marchetti v. United States,* 390 U.S. 38 (1968) and related cases do not support their arguments. Taxpayers' Brief, pp. 23-24. While the Court ruled that criminal prosecution for failure to comply with the wagering tax could be barred by the privilege against self-incrimination, the Court clearly stated that barring criminal prosecution for failure to comply with the tax in no way invalidated the tax itself. For example, in *Marchetti* the Court held:

> *We emphasize that we do not hold that these wagering tax provisions are as such constitutionally impermissible;* we hold only that those who properly assert the constitutional privilege as to those provisions may not be criminally punished for failure to comply with their requirements.

Id. 390 U.S. at 60 (emphasis added).

The Taxpayers apparently view as anomalies the Court's decisions in *United States v. Sanchez,* 340 U.S. 42 (1950) and *Buie v. United States,* 396 U.S. 87 (1969) holding that the Marijuana Tax Act, 26 U.S.C § 4741 et seq. (1954), was a true tax. This view ignores substantial precedent from this Court on the Harrison Narcotic Drug Act of 1914, 38 Stat. 785; 6 U.S. Comp. Stats. 1916, § 6287g. That act placed excise taxes on persons who dealt with opium and coca leaves and their derivatives. For example, it imposed a $300 a pound tax on the manufacture of opium

for smoking purposes. The Harrison Narcotic Drug Act survived a long series of challenges before the Court on various constitutional grounds. See, e.g., *United States v. Jin Fuey Moy,* 241 U.S. 394 (1916); *United States v. Doremous,* 249 U.S. 86 (1919); *Linder v. United States,* 268 U.S. 5 (1925); *United States v. Daugherty,* 269 U.S. 360 (1926); *Nigro v. United States,* 276 U.S. 332 (1928).

In *Jin Fuey Moy* the Court rejected a challenge that the narcotic tax is not a true revenue measure but an unconstitutional exercise of police powers reserved to the states. In *Linder* the Court repeated that holding: "[t]he Narcotic Law is essentially a revenue measure and its provisions must be reasonably applied with the primary view of enforcing the special tax." *Linder,* 268 U.S. at 22. Also see, *United States v. Balint,* 258 U.S. 250 (1922).

The Court also has ruled that governments may tax illegal activity and income from illegal activity even though that income may be forfeited.[8] *James v. United States,* 366 U.S. 213 (1961).

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[8] Nor is it an aberration to tax illegal conduct higher than legal conduct. For example, the federal government currently taxes illegal gambling at two percent of receipts and legal waging at one-quarter of one percent. 26 U.S.C. § 4401(a). See *United States v. Hallmark,* 911 F.2d 399 (10th Cir. 1990) which upheld the tax.

G. The Rate of the Montana Tax and Its Alleged Economic Effect Does Not Make It a Punishment

The Taxpayers essentially argue that the mere size of the tax assessment makes it a penalty.[9] However, the Court has never accepted that argument. The premise that a tax is invalid if so excessive as to bring about the destruction of a particular business has been "uniformly rejected as furnishing no juridical ground for striking down a taxing act." *Magnano Co. v. Hamilton*, 292 U.S. 40, 44 (1934). Also see, *Pittsburgh v. Alco Parking Corp.*, 417 U.S. 369 (1974) and *Alaska Fish Co. v. Smith*, 235 U.S. 44 (1921) to the same effect.

In *Sonzinsky v. United States*, 300 U.S. 506 (1936) the Court approved a tax of $200 on each transfer of a sawed off shotgun, a machine gun, or a silencer despite the fact some of those items sold for as little as $10 in the 1930's.

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[9] The Bankruptcy Court apparently found the Montana Drug Tax excessive in relation to the wholesale price for a pound of "shake." As was noted other federal courts have not found a tax of $100 an ounce so excessive as make the tax a penalty and not a tax. Further, the record shows that the price of shake at retail (1/4 ounce) quantities was more than $100 per ounce. See the "Trans-High Market Quotations" in Tr. Exhs. AA3, AA4, and AA5.

Deputy Saville testified that there was a common simple device, a "marygin," being used by marijuana smokers which allows the user to upgrade the marijuana by separating the stems and seeds from the leaves. Tr. at 253-254.

The Taxpayers used the "shake" to make marijuana oil, a product with a much higher value. Tr. at 78.

Id. at 509. That is, the Court approved a tax 20 times the value of the taxed commodity.[10]

High excise taxes at or over the costs of the commodities have existed since the founding of the nation.[11] The current federal excise tax on distilled spirits is $13.50 per proof gallon. ($10.50 for a gallon of 80 proof (40%) alcohol.) 27 C.F.R. part 19. Raw grain alcohol (95%) currently sells at wholesale for $1.01 to $1.15 per gallon.[12] The Montana and federal excise taxes on cigarettes and cigars greatly exceeds the value of the tobacco in those products.[13]

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[10] The Court held: "[w]e are not free to speculate as to the motives which moved the Congress to impose it, or as to the extent to which it may operate to restrict the activities taxed." *Sonzinsky*, 300 U.S. at 514.

[11] For example, the Excise Act of 1791, 1 U.S. Stat. at Large, 199, enacted a whiskey excise tax of 30 cents per gallon. This tax might seem infinitesimal today until one realizes that a gallon of whiskey in the early 1790's usually cost less than 50 cents. *Taxation in the United States*, R.E. Paul, Little, Brown & Co., Boston, 1954, at 6.

[12] "Oxy-Fuel News Letter," Vol. 5, No. 31. (November 22, 1993, Hart Publications, Arlington, Va.)

[13] The federal excise tax is 1.2 cents per cigarette. 26 U.S.C.S. § 5701 Montana's excise tax is .9 cents per cigarette. Mont. Code Ann. § 16-11-111. According to the United States Department of Agriculture, there is about 1.7 pounds of tobacco in 1,000 cigarettes and the average price of cured tobacco is about $1.90 per pound. "Tobacco Situation & Outlook," Economic Research Service, USDA, TS-216 (Sept. 1991). Thus, the value of the tobacco in a cigarette is about 1/3 of a cent. The current federal excise tax is four times the value of the tobacco in a cigarette. The current Montana excise tax is three times the value of the tobacco.

H. The Circuit Court's and the Taxpayers' Demand That the Department Give a Particularized Accounting of Actual Damages and Costs Caused by These Taxpayers Illustrates Why *Halper* cannot be Applied to the Montana Tax.

The circuit court's requirement for a showing of the "actual costs" and the Taxpayers' demand for an accounting as applied to these individual Taxpayers illustrates the inapplicability of *Halper* to the Montana Tax. The penalty at issue in *Halper* involved fraud on the federal government and was statutorily linked to the damages. In such cases there is an "actual cost," a monetary loss, to the federal government caused by the illegal act in addition to the costs of investigation, trial, etc.

It is difficult to do an accounting of the "actual costs" of drug abuse and trafficking on society apart from those general studies which are in the public record and of which the Court has taken judicial notice. See *Treasury Employees v. Von Raab*, 489 U.S. 656, 688 (1989). The costs of drugs on society are diffused throughout society and defy "particularized" accounting.[14] The cost of illegal drugs on government services is equally diffuse.[15]

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[14] The costs of drugs to society is difficult to estimate. For example, one report is *Economic Costs to Society of Alcohol and Drug Abuse and Mental Illness: 1980*, Research Triangle Institute, June 1984, RTI/2734/00-01FR, Research Triangle Park, North Carolina. In 1980 that report estimated the total direct and indirect cost of drugs on society was almost 47 billion dollars. *Id.* at 4. That report estimated in 1980 the additional costs were public and private criminal justice expenses ($5.9 billion), lost employment of crime victims ($845 million) and the ultimate incarceration of convicted criminals ($1.5 billion). *Id.* at 5.

[15] In 1989 the federal government's best guess was that it spent $6.3 billion dollars on services related to illegal drugs with about $200 million being spent by the federal courts alone. "National Drug Control Strategy, Budget Summary." The White House, 1990 pp. 7-8.

The Taxpayers grew and sold large amounts of marijuana. After their initial sale of the marijuana it is impossible to trace their marijuana to the street where it was finally consumed. The Taxpayers were far removed from the actual consumers whose consumption of marijuana and associated activities result in the societal and governmental costs. Yet, the Taxpayers were the essential initiating cause of all these costs.

Where the sanctioned activity is so removed from the ultimate damages and cost of that activity, the Court's analysis under *Halper* fails. In such instances the more generalized test for sanctions developed by the Court in *United States v. Ward*, 448 U.S. 242 (1980), must be applied. As shown in the Department's first brief at pages 31 through 32 under the standards developed by the Court in *Ward* the Montana Tax is clearly remedial.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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December 1993